



BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

FILED

08-07-06

04:21 PM

Order Instituting Rulemaking to Establish Policies and Rules to Ensure Reliable, Long-Term Supplies of Natural Gas to California.

Rulemaking 04-01-025
(Filed January 22, 2004)

Order Instituting Rulemaking to Require California Natural Gas and Electric Utilities to Preserve Interstate Pipeline Capacity to California.

Rulemaking 02-06-041
(Filed June 27, 2002)

In the Matter of the Application of Southern California Gas Company Regarding Year Six (1999-2000) Under Its Experimental Gas Cost Incentive Mechanism and Related Gas Supply Matters. (U 904 G)

Application 00-06-023
(Filed June 15, 2000)

In the Matter of the Application of San Diego Gas and Electric Company (U 902 G) to Modify and Extend Permanent Gas Procurement Performance-Based Ratemaking Mechanism.

Application 02-10-040
(Filed October 31, 2002)

**COMMENTS OF THE DIVISION OF RATEPAYER ADVOCATES ON
THE PROPOSED DECISION OF ALJ MALCOLM AND PROPOSED
ALTERNATE DECISION OF PRESIDENT PEEVEY**

In accordance with Rules 77.2 and 77.6 of the Rules of Practice and Procedure of the California Public Utilities Commission (“Commission”), the Division of Ratepayer Advocates (“DRA”) hereby submits its comments on the Proposed Decision (“PD”) of Administrative Law Judge Kim Malcolm and the Proposed Alternate Decision of President Peevey (“AltPD”) in the above-captioned proceeding relating to the Winter 2006-07 gas hedging plans of Pacific Gas and Electric Company’s (“PG&E”), Southern California Gas Company (“SoCalGas”) and San Diego Gas & Electric Company (“SDG&E”).

I. THE PROPOSED DECISION APPROPRIATELY RETAINS SOME REASONABLE LEVEL OF UTILITY ACCOUNTABILITY FOR THEIR HEDGING PROGRAMS

DRA supports ALJ Malcolm's PD because it retains some measured level of corporate accountability for the gas utilities' respective hedging activities and proposed winter hedging programs. The PD provides utilities with the option of allocating either 25% or 100% of their hedging costs to their respective incentive mechanisms. By contrast, the AltPD adopts the utility proposed hedging plans without modification and allows the utilities to hedge entirely outside of their respective incentive mechanisms. Thus, the AltPD eliminates any reasonable level of corporate accountability for the utilities' respective hedging plans, provides little or no incentive for the utilities to optimize their hedging decisions or minimize winter hedging costs, and results in excessive risk exposure for core ratepayers. As such, DRA requests that the Commission keep the safeguards provided by the PD regarding corporate accountability.

The Alt PD presumes that the existing incentive mechanisms may not be structured in ways to motivate optimal purchases of hedging instruments on behalf of core customers. (AltPD, Finding of Fact No. 8) Yet, the AltPD provides no evidence regarding how the elimination of corporate risk through approval of utility proposed hedging plans outside an incentive based structure serves to motivate optimal purchases of hedging instruments on behalf of core customers. DRA is concerned that the utilities would not be motivated to make optimal purchases of hedging instruments with all corporate incentive and risk eliminated. ALJ Malcolm's PD recognizes that the blank check approval of hedging expenditures outside the incentive mechanism is surely no elixir to motivate optimal hedging strategies and purchases, and it therefore appropriately allocates a reasonable level of the hedging exposure to the incentive mechanism in order to retain some amount of corporate accountability for hedging decisions.

II. THE APPROVED HEDGING PLANS SHOULD NOT INCLUDE NON-WINTER MONTHS

The Ordering Paragraphs of the PD and the AltPD establish a cap of \$14 per core customer for hedging purchases made during the 2006/2007 **winter season**. However,

neither the PD nor the AltPD define the winter season. The AltPD approves the utility hedging plans and appears to assume that the hedging programs cover only the winter season. DRA presented evidence in its confidential brief that is contrary to such assumption.

In Conclusion of Law (COL) #2 and Ordering Paragraph (OP) #2, the AltPD approves the hedging plans of PG&E, SDG&E, and SoCalGas as follows:

“The hedging plans of PG&E, SDG&E and SoCalGas should be approved, and the request to modify Decisions (D.) 05-10-015, D.04-01-047, D.05-10-043, D.02-06-023 and D.03-07-037 in the manner requested by the utilities should be granted. (AltPD COL #2)

and

“The hedging plans of PG&E, SDG&E and SoCalGas, which are part of their respective petitions and which were filed under seal, are approved.” (AltPD, OP#2)

This blanket approval of the hedging plans is in conflict with the AltPD’s Conclusion of Law 3 which states:

“Since the petitions only seek authority for expanded hedging activities for the **2006-2007 winter**, and are not seeking a permanent change to the incentive mechanisms, today’s expanded hedging authority and modification of D.05-10-015, D.04-01-047, D.05-10-043, D.02-06-023 and D.03-07-037 should be limited to the 2006-2007 **winter season only**. (emphasis added)

The AltPD does not discuss treatment of non-winter month hedging within the context of approving the utility hedging plans. As previously stated, DRA provided evidence that rebuts the presumption that the proposed hedging programs are merely limited to hedging for the “winter season.” In order to be consistent with the intent and discussion within the AltPD and Conclusion of Law #3, DRA recommends that Conclusion of Law #2 and Ordering Paragraph #2 of the AltPD be modified to clarify that the utility hedging plans are approved only with respect to the 2006/2007 winter

months. DRA suggests that the AltPD replace Conclusion of Law #2 with the PD's Conclusion of Law #4 which states:

“The utilities should be authorized to account for hedging activities outside the incentive mechanisms only for purchases that cover gas costs during winter months.”

Likewise, DRA recommends that Ordering Paragraph #2 of the AltPD should be clarified as follows:

“The hedging plans of PG&E, SDG&E and SoCalGas which are part of their respective petitions and which are filed under seal, are approved, for winter month hedging only.”

These modifications will ensure consistency within the AltPD's approval of 2006/2007 winter season hedging.

III. SWAPS AND THE \$14/CUSTOMER CAP FOR THE WINTER SEASON

Both the PD and the AltPD state in several places that “[the \$14 per customer] limitation does not include hedging instruments commonly known as swaps.” The PD offers ratepayers some risk protection and utility accountability for swaps through the inclusion of 25% hedging risk in the utility incentive mechanism. (PD, Ordering Paragraph 1.) However, the AltPD embraces the hedging plans as filed, suggesting that utilities may engage in swaps that can result in costs and ratepayer exposure well beyond the \$14 per customer limitation. The AltPD places no caps on losses due to swaps. Merely because swaps do not entail any significant up-front costs, it does not mean that swaps provide a free ride. In fact, swaps can be viewed consistent with fixed-price contracts and can expose ratepayers to significant risk. As described in DRA's May 26, 2006 Response to PG&E's Petition, swaps can result in significant exposure and losses for core ratepayers. The AltPD fails to discuss or identify these risks and the possible additional impact on rates over and above the \$14/customer limitation.

DRA assumes that the AltPD intended to provide core ratepayers with a risk limitation, as implied by the approval of the lower of the amount requested in their respective hedging plans or up \$14 per customer for the 2006/2007 winter season. Yet, by excluding swaps from the limitation, ratepayers are left exposed to risk that can be well in excess of the \$14/customer that the AltPD seeks to authorize for hedging purposes. It appears that the AltPD violates its own implied intent of limiting ratepayer losses.

One utility, within its filed hedge plan, identified a finite ratepayer exposure or cap on swap losses. On the other hand, the other utilities proposed no ratepayer cap on swap limit losses in their plans, as filed. In order for ratepayers to be protected through a cap on hedging costs, DRA recommends that the AltPD be modified to include swaps within the \$14 per customer hedge cost.

IV. CONCLUSION

DRA recommends that ALJ Malcolm's PD be adopted as it seeks to equitably protect both utilities and core ratepayers through the 75%/25% (ratepayer/shareholder) sharing of hedging related risk. In the event the Commission is inclined to adopt the AltPD, it should be modified to either exclude swaps from the approved utility hedging plans or include them within the authorized \$14 per customer hedge cost limitation. In

///

///

///

this manner, ratepayers can be assured a limit on their hedge-related risk exposure. The AltPD should also be modified to approve the utility hedging programs only to the extent that hedging instruments are related to months within the 2006-2007 winter season.

Respectfully submitted,

/s/ RASHID RASHID

RASHID RASHID

Staff Counsel

Attorney for the Office of Ratepayer
Advocates

California Public Utilities Commission
505 Van Ness Ave.

San Francisco, CA 94102

Phone: (415) 703-2705

Fax: (415) 703-2262

August 7, 2006

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of COMMENTS OF THE DIVISION OF RATEPAYER ADVOCATES ON THE PROPOSED DECISION OF ALJ MALCOLM AND PROPOSED ALTERNATE DECISION OF PRESIDENT PEEVEY in R.04-01-025, R.02-06-041, A.00-06-023 and A.02-10-040 by using the following service:

[X] **E-Mail Service:** sending the entire document as an attachment to all known parties of record who provided electronic mail addresses.

[] **U.S. Mail Service:** mailing by first-class mail with postage prepaid to all known parties of record who did not provide electronic mail addresses.

Executed on August 7, 2006 at San Francisco, California.

/s/ CHARLENE D. LUNDY

Charlene D. Lundy

N O T I C E

Parties should notify the Process Office, Public Utilities Commission, 505 Van Ness Avenue, Room 2000, San Francisco, CA 94102, of any change of address and/or e-mail address to insure that they continue to receive documents. You must indicate the proceeding number on the service list on which your name appears.

* * * * *

Service List for R.04-01-025, R.02-06-041, A.00-06-023, A.02-10-040

jtisdale@arclightcapital.com
keith.mccrea@sablaw.com
roger@berlinerlawpllc.com
swilliams@desc.dla.mil
jimross@r-c-s-inc.com
douglas.w.rasch@exxonmobil.com
agold@coral-energy.com
wgarrettesi@aol.com
steve.koerner@el Paso.com
richard.stapler@kernrivergas.com
david.brooks@state.nm.us
andy.bettwy@swgas.com
anita.hart@swgas.com
randy.gabe@swgas.com
bmusich@semprautilities.com
jellis@sempra.com
lurick@sempra.com
mthorp@sempra.com
dgilmore@sempra.com
hchoy@isd.co.la.ca.us
dhuard@manatt.com
pucservice@manatt.com
astele@hanmor.com
npedersen@hanmor.com
klatt@energyattorney.com
douglass@energyattorney.com
liddell@energyattorney.com
kwiese@aqmd.gov
gloria.ing@sce.com
walker.matthews@sce.com
cory@briggslawcorp.com
burkee@cts.com
amsmith@sempra.com
gbaker@sempra.com
lbiddle@ferrisbritton.com
srahon@semprautilities.com
jleslie@luce.com
cscolastico@cc.sbcounty.gov
thunt@cecmail.org
mdjoseph@adamsbroadwell.com
marcel@turn.org
ljt@cpuc.ca.gov
ek@a-klaw.com
sdhilton@stoel.com
scarter@nrdc.org
jkarp@whitecase.com
j1pc@pge.com
kts1@pge.com

rbm4@pge.com
jwmctarnaghan@duanemorris.com
epoole@adplaw.com
bcragg@gmssr.com
chrishilen@dwt.com
enriqueg@lif.org
jarmstrong@gmssr.com
mfogelman@reedsmith.com
mday@gmssr.com
frl3@pge.com
raveen_maan@city.palo-alto.ca.us
Service@spurr.org
kowalewskia@calpine.com
joe.paul@dynegy.com
wbooth@booth-law.com
tomb@crossborderenergy.com
sberlin@mccarthylaw.com
chrism@mid.org
jeff@jbsenergy.com
matt@bradylawus.com
steveng@destrategies.com
creheis@wspa.org
dcarroll@downeybrand.com
dkk@eslawfirm.com
glw@eslawfirm.com
rob@clfp.com
scohn@smud.org
mpa@a-klaw.com
pinney@capp.ca
margaret_crossen@transcanada.com
DSchlissel@synapse-energy.com
ramage@pwlng.com
jbushee@sablaw.com
jcm@vnf.com
pik@vnf.com
eyussman@knowledgeinenergy.com
ralph.dennis@constellation.com
ron.giteck@state.mn.us
alex.goldberg@williams.com
ghinners@reliant.com
edgar.kuipers@shell.com
Larry_Jenkins@oxy.com
kelly.allen@panhandleenergy.com
hobs@bp.com
marzmj@bp.com

bud_becker@kindermorgan.com
michael.crumley@elpaso.com
william.tomlinson@elpaso.com
pesposito@cbcatalysts.com

kjsimonsen@ems-ca.com
sslavigne@duke-energy.com
john.smith@kernriversgas.com
kirk.morgan@kernriversgas.com
Ned.Greenwood@questar.com
djones2@chw.edu
Phyllis@abqenergy.com
dnorris@sppc.com
elizabeth.douglass@latimes.com
cfaber@semprautilities.com
centralfiles@semprautilities.com
robert.pettinato@ladwp.com
pucservice@manatt.com
curtis.kebler@gs.com

sendo@ci.pasadena.ca.us
eklinkner@ci.pasadena.ca.us
slins@ci.glendale.ca.us
jackmack@suesec.com
bjeider@ci.burbank.ca.us
ffletcher@ci.burbank.ca.us
lparker@ci.burbank.ca.us
rmorillo@ci.burbank.ca.us
mkay@aqmd.gov
case.admin@sce.com
david.vaniderstine@sce.com
douglas.porter@sce.com
Michael.Alexander@sce.com
asullivan@sempra.com
wtobin@sempraglobal.com
lwrazen@sempraglobal.com
snelson@sempra.com
mshames@ucan.org
ygross@sempraglobal.com
scottanders@sandiego.edu
mmilner@coral-energy.com
ofoote@hkcf-law.com
ctoca@utility-savings.com
hoffmang@sbcapcd.org
elaine.duncan@verizon.com
mzafar@semprautilities.com
nsuetake@turn.org
clarence.binninger@doj.ca.gov
dwang@nrdc.org
filings@a-klaw.com
mdm8@pge.com

kjbh@pge.com
placourciere@thelenreid.com
norman.furuta@navy.mil

Cem@newsdata.com
daniel.fessler@hklaw.com
james.booth@hklaw.com
smalllecs@cwclaw.com
mmattes@nossaman.com
smalllecs@cwclaw.com
salleyoo@dwt.com
judypau@dwt.com
lisaweinzimer@sbcglobal.net
cpuccases@pge.com
ecrem@ix.netcom.com
lkl1@pge.com
2DMr@pge.com
John.cioffi@ps.ge.com
todp@chevron.com
editorial@californiaenergycircuit.net
JerryL@abag.ca.gov
ceyap@earthlink.net
paulfenn@local.org
mrw@mrwassoc.com
carriec@greenlining.org
robertg@greenlining.org
samuelk@greenlining.org
rcamacho@ci.santa-clara.ca.us
cpechman@powereconomics.com
kswain@powereconomics.com
bmcc@mccarthy.com
gregp@mid.com
wgmanuel@tid.org
jweil@aglet.org
rmccann@umich.edu
cmkehrrein@ems-ca.com
cpucrulings@navigantconsulting.com
gpickering@navigantconsulting.com
roechsler@navigantconsulting.com
karl@ncpa.com
mclaughlin@braunlegal.com
curt.barry@iwpnews.com
kdw@woodruff-expert-services.com
mlgillette@duke-energy.com
blaising@braunlegal.com
cabaker906@sbcglobal.net
kmills@cbbf.com
karen@klindh.com
bbrunel@smud.org

david_white@transcanada.com
leslie_ferron-
jones@transcanada.com
egw@a-klaw.com
lscott@landsenergy.com

loe@cpuc.ca.gov
agc@cpuc.ca.gov
beg@cpuc.ca.gov
dkf@cpuc.ca.gov
dre@cpuc.ca.gov
dil@cpuc.ca.gov
cpe@cpuc.ca.gov
hym@cpuc.ca.gov
jnm@cpuc.ca.gov
jsw@cpuc.ca.gov
alf@cpuc.ca.gov
kcl@cpuc.ca.gov
kim@cpuc.ca.gov
lau@cpuc.ca.gov
mxh@cpuc.ca.gov
nil@cpuc.ca.gov
rxr@cpuc.ca.gov
ram@cpuc.ca.gov
rmp@cpuc.ca.gov
rle@cpuc.ca.gov
skh@cpuc.ca.gov
saw@cpuc.ca.gov
wmp@cpuc.ca.gov
dsimerot@arb.ca.gov
gyee@arb.ca.gov
aulmer@water.ca.gov
bill.julian@sen.ca.gov
edward.randolph@asm.ca.gov
Jim.Campion@conservation.ca.gov
mpurcell@energy.state.ca.us
Mschwebs@energy.state.ca.us
jgopal@energy.state.ca.us
jgeorge@water.ca.gov
jpacheco@water.ca.gov
Sphinney@aspeneg.com